ENVIRONMENTAL ENTREPRENEURS

www.e2.org

<u>Via e-mail to climatechange@calepa.gov</u>
Winston Hickox
Chair, Market Advisory Committee

Re: Comments on the Market Advisory Committee's Draft Report

June 14, 2007

Dear Chairman Hickox and Committee members:

On behalf of Environmental Entrepreneurs (E2), thank you for your hard work in putting together draft recommendations to help inform the California Air Resources Board's (CARB) policymaking process.

E2 is engaged in discussions with many business organizations, clean tech companies, and biofuels companies about the pros and cons of different market mechanisms as policy tools to reduce greenhouse gas (GHG) emissions in California. These comments represent our preliminary views. In general, E2 supports many of the draft report's recommendations, and we focus our comments and suggestions on aspects of the draft report that we believe could be improved upon to design a program that is in the best interest of California and meets the requirements of AB 32. This includes achieving real emission reductions, providing net economic benefits, not disproportionately impacting low-income communities, and complementing state efforts to improve air quality and reduce toxic emissions.

In summary, we urge you to revise the draft report to:

1) Emphasize that the stringency of the cap is the main driver of reductions.
2) Recommend that offsets should be limited.
3) Recommend that allowances should not be grandfathered.
4) Urge that both the "load-based" and "first seller" approaches in the electricity sector should be analyzed.
5) Recommend that the Point of Regulation should be with those who can change their business practices.

Stringency of the Cap is the main driver of reductions.
The benefits of a cap and trade program can only be realized if the cap is set tightly enough to achieve real emission reductions. A strong cap will guarantee that California meets the 2020 emission reduction targets.

We are aware that some alarms have been rung about cap and trade programs. We believe that the MAC could assuage some of the apprehension that exists by explaining in more detail that the cap from the cap and trade program is the main policy instrument that will drive reductions and guarantee that California meets its 2020 target. Trading is merely a mechanism for ensuring that those reductions are cost-effective.

Offsets Should Be Limited
We believe that offsets should only be considered if a strong and enforceable cap is set. We urge the MAC to recommend that if offsets are allowed, they should be limited to a portion of the compliance obligation and to project types that will provide environmental and economic co-benefits to California. One of the benefits of offsets is that they can create liquidity in a carbon market. We would like to see more information on the pros and cons of offsets in the revised draft report.

Allowances Should Not Be Grandfathered
We urge the MAC to explicitly recommend that allowances not be grandfathered. We support the Committee's recommendation that "there should be no free allocation to firms under the cap that are able to pass most of their costs on to consumers." (p.53) We support auctioning permits. Auctions offer a price signal and will encourage early action.

Both the "Load-Based" and "First Seller" Approaches in the Electricity Sector Should be Analyzed
Without a more detailed side-by-side comparative analysis, it is not possible to determine whether a "load-based" or "first seller approach is best for California. The MAC's recommendation of a first-seller approach appears to rest strongly on the assumptions that a first seller approach will be easier to transition into a national program and that CARB will be able to track the first sellers of electricity into the state and provide the appropriate enforcement. While a smooth transition to a national program is a worthy goal, a more detailed comparison of the pros and cons of each approach is required.

We believe that load-based entities are more likely to create business changes which can reduce GHG and that first sellers will have less flexibility in their business operations and thus will pass all costs on to their customers.

Point of regulation should be with those who can best change their business practices
Though Program 4 is attractive because it includes a small number of entities with large coverage, the upstream entities are least likely to change their business practices. If you are a natural gas importer, there isn't much you can do to make your product less GHG intensive. On the other hand, a public utility has a great deal of choice in their business operations and enough capital to make changes. For this reason, we believe that Option A (Beginning with Program 1 and progressing to Program 2 and 3) is more desirable that Option B (i.e., starting with Program 4).

Thank you for considering these suggestions as you finalize your recommendations to CARB.

Sincerely,

Bob Epstein
Co-founder
Environmental Entrepreneurs